

Service Date: November 12, 1991

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of the Application)	UTILITY DIVISION
by the MONTANA POWER COMPANY for)	DOCKET NO. 90.6.39
Authority to Increase Rates for)	ORDER NO. 5484p
Natural Gas and Electric Service.)	(REVENUE REQUIREMENT)

ORDER ON MOTIONS FOR RECONSIDERATION

INTRODUCTION

On July 19, 1991, the Commission issued Order No. 5484k, the Final Order on revenue requirement in this Docket. On or around July 30, 1991, the Commission received motions for reconsideration (and accompanying briefs) of Order No. 5484k from the Montana Power Company (MPC), the Montana Consumer Counsel (MCC), and District XI Human Resource Council (HRC). On August 13, 1991, the Commission received response briefs from MPC and MCC. After careful consideration, the Commission responds and disposes of the motions as described below.

FINDINGS OF FACT

Capital Structure

1. MCC notes that the Commission found that the Leveraged Employee Stock Ownership Plan (LESOP) shares are entitled to the same return as other MPC shares of common equity. MCC claims that the real issue is whether ratepayers should pay both the dividend paid to the trustee plus the retained earnings amount that MPC keeps. MCC states that under the proposal accepted by the Commission, ratepayers pay both dividends and retained earnings. MCC states that at the same time, MPC pays the interest to the

institutional investors approximately equal to the dividend portion and retains the rest for the benefit of shareholders. MCC claims that the true cost of the LESOP is the interest paid to the institutional investors. MCC argues that the retained earnings portion represents funds confiscated from ratepayers.

2. MCC then concludes that at the very least the Commission should reduce equity to account for the 19 percent of the LESOP that benefits Entech employees. MCC states that such costs are not part of the utility's cost of service and should not be allowed.

3. MPC claims that MCC's motion presents a new argument on this issue. MCC states that the LESOP shares are fully outstanding. MPC argues that MCC is wrong when MCC states that LESOP retained earnings are retained by MPC for other shareholders. MPC claims that such retained earnings belong to the owners of the LESOP stock just as with any other owners of stock. MPC states that various trustees hold MPC stock, that such stock is still outstanding and that all outstanding shares must have the opportunity to earn the equity rate of return.

4. MPC states that the Entech LESOP shares have already been removed as demonstrated in MPC Exh. 29, Exh. WCV-3, pages 3 and 8:

Investment in Entech (WCV-3, p.8)	\$212,454,679
Entech LESOP contra-equity (WCV-3, p.8)	<u>7,478,617</u>
Entech Equity Eliminated (WCV-3, p.3)	\$219,933,296

5. By entering into the LESOP transaction, MPC was able to provide increased benefits to its employees while significantly

reducing MPC's costs through the tax deductibility of dividends paid on LESOP shares. The transaction is essentially a prefunding of MPC's future matching contribution obligations under MPC's deferred savings plan. The LESOP shares remain outstanding and are entitled to an opportunity to earn the same return (dividends and retained earnings) as all other shares of MPC stock. MCC's claim that the Entech portion of the LESOP shares must be removed is incorrect. MPC clearly demonstrated that the Entech portion has already been removed. MCC's motion is denied.

Return on Equity

6. MPC and MCC both requested reconsideration of the authorized return on equity. MPC claims that the 12.1 percent authorized in Order No. 5484k is insufficient while MCC argues it is excessive.

MPC's Motion

7. MPC argues in its motion for reconsideration that the 12.1 percent allowed return on equity is too low. The Company believes the Commission's Order "arbitrarily and capriciously rejects the unrebutted evidence" regarding Montana's regulatory risk and the Company's financial integrity.

8. **Regulatory Risk** - MPC claims that the Commission ignored MPC's regulatory risk arguments. MPC claims that because the Commission found that the impact of regulatory risk on the cost of equity was not quantified, the Commission ignored such risks in setting MPC's allowed equity rate of return. The Company also claims that when the Commission found MPC's regulatory risk analysis to not be a comprehensive analysis of all major risks faced by the utility, the Commission ignored Duquesne Light Co. v. Barasch, 488 U.S.____, 190 S.Ct. 609, (1989). MPC states also

that the record shows the average return allowed in the recent past in other jurisdictions is 12.77 percent. MPC believes that given its regulatory risk analysis, this average return must be factored into MPC's equity return.

9. MCC's response brief points out that the Commission adjusted MPC's recommended return to remove the impacts of financing costs only, with no such adjustment to remove the impacts of MPC's regulatory risk argument.

10. The Commission reiterates that from a philosophical standpoint risk analysis must be comprehensive and that MPC's risk analysis was not comprehensive. Presumably, Dr. Olson included regulatory risk impacts in his recommended return on equity. If that presumption is incorrect, it would indicate that Dr. Olson does not believe his own testimony. Given that the Commission did not adjust MPC's authorized return to remove the regulatory risk impacts, this part of MPC's motion is baseless.

11. Regarding the relevance of returns granted in other jurisdictions, the Commission notes that the records in each of those cases are unique as evidenced by the different returns granted in each jurisdiction. The range of returns runs generally from 12 to 13 percent, with one outlier at 15.76 percent. Additionally, the information contained in the records of those other proceedings is from an earlier time period than in this case which creates a mismatch in comparing those returns with the 12.1 percent authorized in this proceeding. Therefore, the Commission cannot place significant weight on those returns in its deliberation of the evidence in this proceeding.

12. **Financial Integrity** - MPC claims that the Commission made a summary and arbitrary rejection of uncontested evidence

concerning the financial implications of the overall rate decision. MPC believes that the Commission's skepticism toward budgeted information represents insufficient grounds for the Commission to ignore MPC's end results test. MPC states that there was full opportunity for discovery regarding the budgeted information, and that there is no evidence in the record which shows its analysis is flawed or that the budgeted information is unreliable. MPC contends that the Hope and Bluefield decisions constitutionally require that the actual impact on the utility be analyzed to determine if the resulting return is reasonable. MPC states that a budgeted (forecasted) period must be used to determine the actual impact because that is the period in which rates will be in effect.

13. MPC claims that the budgeted information shows that the return on equity allowed by the Commission will not allow MPC to meet the financial tests. MPC states that even with the full increases requested the bond ratings would not reach an A rating. MPC contends that because the allowed increases were well below those requested, "the conclusion is inescapable that the result will likely be downward pressure on the current bond rating, which is already unreasonably low as explained in Mr. Verbael's testimony."

14. MCC responds that the Commission's rejection of budgeted information is entirely proper. MCC explains that acceptance of MPC's position would in every rate case result in an adjusted test year analysis followed by a review of budgeted information to determine the effects on the Company. MCC echoes Order No. 5484k by stating that budgeted information uses many assumptions which clearly are not known and measurable and

analysis of such assumptions would be costly, time consuming and redundant.

15. MCC notes that the Commission sets rates based on an historical test year, not a forecasted test year. MCC states that discovery was not conducted on budgeted information because there is no reason for such discovery given the use of an historical test year.

16. MCC disagrees with MPC's claim that the Company's bond rating is unacceptably low. MCC observes that MPC's bonds are rated investment grade and MPC's claim that the its bond rating is too low is not supported in the record.

17. The Commission continues to believe that its rejection of MPC's budgeted information is proper. MPC's budgeted information in no way reflects the validity of this Commission's ratemaking decisions. The MPC budgeting process reflects costs that this Commission has specifically found are not properly recoverable from ratepayers. To accept MPC's position would be akin to accepting a future test year with no analysis of the propriety of components of that future period. MPC's argument also ignores Docket No. 91.6.24 in which MPC filed for and received additional revenues of \$1.7 million to cover period QF cost increases.

18. MPC makes a claim which is not supported by the record. MPC contends that because the allowed increases were well below those requested, "the conclusion is inescapable that the result will likely be downward pressure on the current bond rating, which is already unreasonably low as explained in Mr. Verbael's testimony." The record information indicates that Mr. Verbael

opined that interim revenues would support the low side of a BBB rating and that MPC's own proposed rates would probably not support an A rating. MPC ignores the fact that the aggregate increase is also well above the interim levels which could place upward pressure on MPC's financial benchmarks. There is no information on the record showing that the authorized revenues will cause downward pressure on MPC's bond ratings. MPC's bonds are investment grade and in the Commission's opinion its utility financial benchmarks support the current BBB+ bond rating.

19. Based on the above discussion of MPC's regulatory risk and financial integrity arguments, the Commission finds insufficient reason to increase MPC's authorized equity rate of return. MPC's motion is denied. MCC's Motion

20. MCC argues in its motion for reconsideration that the 12.1 percent allowed return on equity is too high. MCC believes that the Order does not adequately explain how the Commission arrived at the allowed return on equity.

21. MCC states that the Commission agreed with MCC on financing cost adjustments, the sensitivity of Dr. Smith's model and the results of operations test. MCC states that the Commission did not criticize Dr. Smith's methodology anywhere in the Order.

22. MCC claims that the Commission did not specify the information relied on to arrive at the allowed 12.1 percent return on equity. MCC contends that this leaves parties with no clear direction on how the Commission believes cost of equity recommendations should be made in future proceedings. MCC states that the Commission has accepted Dr. Smith's methodology for the

past ten years and effectively rejected it in this proceeding without explanation.

23. MCC presents the most recent Federal Energy Regulatory Commission (FERC) generic rate of return on equity of 11.72 percent as support for the MCC recommendation. MCC claims that the record clearly indicates that MPC is less risky than the average utility and that allowing 40 basis points above the FERC benchmark would result in unwarranted overcharges to ratepayers.

24. MPC responds that MCC's presentation of the FERC generic rate of return is an improper attempt to introduce new information after the record has been closed. MPC cites a previous case before this Commission in which MDU's attempt to introduce a bond chart after the close of the hearing was denied by the Commission. MPC states that at no time during the case did MCC present evidence regarding the applicability of the FERC generic rate of return in determining a reasonable return for MPC. MPC mentions that the FERC rate has been and still is higher than that proposed by MCC. MPC states that given the opportunity, MPC would show that the FERC benchmark is rarely used by FERC, and that in the rural electric co-op case the FERC staff proposed a 12.4 percent return for MPC and concluded MPC is more risky than other comparable utilities.

25. MPC states that the new FERC benchmark is for filings made during August through October and thus creates a mismatch because all evidence in the case relates to the period prior to 1991. MPC states that the test period and data used by Dr. Olson and Dr. Smith relate to a different period, and a new FERC benchmark should not be compared to that period.

26. MCC in its motion appears to be asking the Commission to tell it how to make return on equity recommendations in future cases. This would be a step in the direction of prejudging an issue in future cases, something this Commission will not do.

27. The Commission finds that the introduction of the FERC benchmark is improper because the record in this proceeding is closed. The Commission will not consider the FERC benchmark in this proceeding.

28. Regarding MCC's other arguments, the Commission is not persuaded that the authorized equity rate of return is excessive. The Commission found parts of both Dr. Smith's and Dr. Olson's testimony to be valid. Therefore, both witnesses' positions weighed heavily in arriving at the 12.1 percent authorized equity rate of return for MPC. The Commission, after much deliberation, reached a return on equity determination that it believes is fair to both the Company and the ratepayers. MCC's motion is denied.

Captive Coal

29. MPC's motion claims that while the Order states that a reasonable return on equity for Western Energy Co. (WECo) should be based upon cost of capital, the return was not based on any cost of capital, and that MCC provided no evidence on cost of capital for the coal industry. MPC states that MCC's analysis was based on historical earned returns, which all parties agreed is not the same as the cost of capital. MPC claims that Dr. Wilson and Mr. Quinlan agreed that there were insufficient data to perform a cost of capital analysis for the coal industry.

30. MPC believes that the only tie to cost of capital was Dr. Wilson's reference to the MCC proposed utility rate of return. MPC states that while it disagrees with equating the

utility cost of capital with the coal industry cost of capital, the Commission ignored the only cost of capital evidence available when the Commission did not adjust the coal return in relation to that determined for the utility operations.

31. MCC states that, contrary to MPC's motion, the MCC testimony clearly and extensively addressed WECO's cost of capital. MCC states that the primary cost of capital analysis used by Dr. Wilson was comparable earnings analysis. MCC states that the most fundamental of all cost of capital principles is the tenet that the cost of capital is the rate of return which could be earned on investments of comparable risk. MCC states that Order No. 5484k clearly addressed comparable risk. As an example, MCC cites the Commission's recognition that WECO's unleveraged capital structure reduces financial risk and allows WECO to earn an equity return on the entire earnings base.

32. The Commission finds that MPC incorrectly concluded that no cost of capital analysis was performed and that the witnesses agreed the data were not adequate to perform cost of capital analysis. In actuality, the witnesses agreed that **discounted cash flow (DCF) analysis** could not be conducted due to the inadequacy of the data for coal companies. DCF analysis is one of several methods for estimating cost of capital, including risk premium analysis, the capital asset pricing model and **comparable earnings analysis**. DCF analysis is the Commission's preferred method in estimating cost of capital, but it clearly is not the only method available to estimate cost of capital. As stated in the MCC Reply Brief:

The most fundamental of all cost of capital principles, explicitly embodied in virtually all legal precedents dealing with fair return allowances, is that the cost

of capital is that rate of return which an investor would be able to realize from an alternative investment of comparable risk. (MCC Reply Brief, p. 4)

The Commission decision also considered WEC's business and financial risks. (Order No. 5484k, FOF 108-109) MPC's motion is denied.

Hydro Peak Capability

33. MPC's motion asks the Commission to reconsider its hydro peak capability decision. MPC believes that it has presented a complete description of hydro peak capability in Mr. John Leland's direct testimony. MPC states that no party contested its study and that there is no evidence in the record to refute the study. MPC thus believes that the Commission's decision is not based on the record as required by both Constitutional due process and the Montana Administrative Procedure Act. MPC further argues that the Commission did not give the Company any opportunity to respond to the charge in Order No. 5484k.

34. Next, MPC points out that the Commission's decision has a profound impact on MPC's resource planning even though there is no revenue requirement impact resulting from the Commission's decision. MPC explains that it will acquire resources in the next year, and the Commission's decision will reduce its acquisition of peak resource by approximately 30 MW. As a result, MPC believes it may be forced to forgo cost-effective resources. In conclusion, MPC asks the Commission to accept its hydro peak capability proposal.

35. MCC asks the Commission to reject MPC's procedural fairness arguments. MPC claims that the Commission has recognized the difference between administrative and judicial decision-

makers. MCC argues that the Commission is not bound by the positions and recommendations of parties but, on the contrary, has an obligation to analyze MPC's requests. MCC believes that MPC's argument that the Commission cannot respond to this issue is incorrect.

36. Next, MCC suggests the Commission withdraw any conclusions on the hydro peak capability issue in this Order. MCC states that since MPC admits that there is no revenue requirement impact, the company can revisit the issue in future cases.

37. The Commission finds merit in MCC's proposal to withdraw the conclusions on hydro peak capability from Order No. 5484k. The Commission agrees with MCC's point that since there is no revenue requirement impact in this rate case, the hydro peak capability issue should be addressed in the next rate case if MPC's revenue requirement is impacted by its resource planning at that time. In other words, the Commission finds that this is a resource planning issue rather than a revenue requirement issue in this Docket. By withdrawing its findings on this issue, the Commission expresses no opinion on the due process objections made by MPC at pages 8-14 of its opening brief on reconsideration.

Test Year vs. Forecast Year loads

38. MCC requests that the Commission reconsider its findings regarding the test year loads mismatch, noting the Commission's reasons for rejecting MCC's adjustment are not supported.

39. First, MCC believes that to totally reject MCC's adjustment is tantamount to saying that there are no sales associated with a load growth of 20 aMW. MCC petitions the

Commission to reprice the residual energy from the Idaho Power (IP) purchase after the sale to Washington Water Power (WWP).

40. Second, Finding of Fact 187 states that it is inappropriate to make a forward-adjustment to test year loads. MCC argues that the expenses associated with the forecast (or forward-adjusted) load have been allowed by the Commission in the IP purchase expense. MCC believes that since the Commission included the IP purchase expense, it should also include the increased revenue from the IP purchase. MCC advises the Commission to address the loads mismatch by repricing the residual energy of the IP purchase at firm sales prices.

41. Third, MCC states that MPC acquired both a peak and energy resource through the purchase contract which does not provide for separate capacity and energy payments. MPC believes that the IP purchase created residual firm energy. Therefore, MCC argues that the residual energy of the IP purchase after the WWP sale should be priced at a firm price. MCC concludes that if this is not done, the Commission will have allowed MPC to acquire a firm resource to serve non-firm load.

42. MPC disagrees with MCC's motion for reconsideration on the issue of the test year loads mismatch. In its motion, MCC contends that the residual energy of the IP purchase after the WWP sale should be priced at a firm price. MPC states that this is precisely what the Company has done. MPC claims that "all of the energy associated with Idaho purchase has been priced out at firm, off-system prices -- the WWP and Pacificorp prices." Thus, MPC believes that "The MCC's own criteria has been met."

43. The Commission denies MCC's motion for reconsideration of the test-year loads mismatch in this proceeding. The

Commission finds that the test-year loads mismatch and the repricing residual IP energy are two different issues. The Commission finds that there is no relation between repricing residual energy and the forecast energy loads. The loads mismatch involves two loads -- the test year loads and the forecast loads, and the question is how to deal with the loads mismatch. The residual energy sale involves MPC's residual energy from the IP purchase and the question is how to sell this residual energy to increase the test year revenue. The residual energy is caused by the IP purchase not the forecast energy loads, even if the forecast energy loads are higher than the test year loads. In other words, the Commission finds that, aside from the loads mismatch adjustment, as far as the IP purchase is concerned, residual energy from the IP purchase will exist. Whenever a utility (like MPC in this case) acquires capacity, energy is unavoidably provided. The Commission agrees with MCC's point that the payment for the IP purchase includes both capacity and firm energy. The Commission thus believes that the key point here is whether the residual firm energy is sold at the firm price to increase test year revenues. The Commission will address this question in the issue of repricing the residual energy sale. For these reasons, the Commission finds that both MPC and MCC are logically incorrect to relate the loads mismatch issue to the repricing residual energy issue in this Docket.

44. The Commission finds that the test year load mismatch issue has changed since MCC filed its original testimony. Initially Mr. Drezmiecki proposed an adjustment to reprice 20 aMW at the system average revenue per kwh as opposed to the monthly

off-system sales prices. This adjustment would have increased MPC's revenues by \$4,035,769.

45. In its initial brief MCC changed its argument to reflect the fact that the 20 aMW amount included an element for losses associated with non-firm off-system sales. As a result MCC stated that the adjustment for residual energy needed to be scaled back. This revised adjustment would increase MPC's revenues by \$2,712,397.

46. In Order No. 5484k the Commission found that the IP purchase was needed to serve peak loads in the test year. There is no evidence to the contrary on this record. As to the energy associated with the IP purchase, the Commission finds that all of the energy was sold at firm off-system prices to Washington Water Power and PacifiCorp. The response to HRC Data Request No. 1 indicates that the net cost of the IP purchase is \$478,260 after reflecting the sales to WWP and PacifiCorp. If MCC's revised adjustment were accepted, the net effect of the IP purchase would be a decrease in MPC's revenue requirement of \$2,234,137 (\$478,260 - \$2,712,397), which is an unreasonable outcome. MCC's proposed test year repricing adjustment is denied.

PacifiCorp Sale Repricing

47. MCC in its Motion for Reconsideration recommends that the Commission reprice the energy sold to PacifiCorp using the price of 29.81 mills per kwh from the sale to the Los Angeles Department of Water and Power (LADWP), or the price of 28.1 mills per kwh from the Puget sale. MCC stated that it is patently obvious that the utility could have served a portion of either the LADWP or Puget sale to the extent that it was already serving the PacifiCorp sale. However, MPC in its reply comments stated

that it is not true that MPC could simply have provided power for the Puget or LADWP sale for five years and received the same price. The Commission finds that there is no evidence that MPC could have sold power to LADWP or Puget for five years at the same prices that are included in those contracts due to the difference in the terms of those sales.

48. In Order No. 5484k, the Commission found that comparing the PacifiCorp sale to the LADWP or Puget sale is not valid due to the difference in load factors in the contracts. The order noted that if the load factors in either the LADWP or the Puget sales are set at 100 percent as the PacifiCorp sale is, the result of the comparisons indicate that repricing the PacifiCorp sale as recommended by Mr. Clark would have a negative impact on ratepayers. In MCC's Motion for Reconsideration there is a footnote which states:

While it may be true that the revenues have to be stated on the same basis for purposes of an adjustment, comparisons are clearly possible with such a restatement.

This statement in the MCC Motion affirms the decision reached on the issue of the PacifiCorp Sale Repricing in Order No. 5484k. The Motion for Reconsideration by MCC is denied.

Reciprocal Sharing Agreement

49. MPC requests that the Commission reconsider its procedure for further addressing the reciprocal sharing agreement (RSA) between Colstrip 3 and 4 and to adopt an alternative procedure as suggested by MPC. MPC objects that the Commission is attempting to force MPC to prove a negative (that rates should not be reduced as a result of the RSA). MPC contends that either the Commission or a party proposing an adjustment in rates must

carry the burden as indicated in Sections 69-3-321, 324, MCA. MPC also argues that Order No. 5484k is too vague, and does not make clear what MPC is required to do in the October 1, 1991, filing (extended to January 30, 1992). MPC proposes, as an alternative to the Commission directed procedure, that it prepare the requested life cycle cost analysis along with a narrative description of the analysis. MPC would also be available to answer questions, and if as a result any party (or the Commission staff) thinks some Commission action is required, then that party would go forward using the statutory complaint procedure.

50. The Commission finds that MPC's objections to the RSA procedure are substantially without merit. The Commission also finds, however, that MPC's objections indicate a need to clarify paragraph 206 and to explain the nature of the RSA proceeding.

51. First, because "burden of proof" is a legal term of art that is difficult to understand and apply in a judicial setting, let alone an administrative setting, the Commission withdraws its finding that MPC has not met its burden of proof with respect to the RSA¹. The Commission asserts, however, that MPC has a burden (task, obligation, responsibility) in all rate cases of persuading the Commission that approval of its various actions is consistent with the establishment of just and reasonable rates. With respect to this matter, that burden involves making a satisfactory explanation of the impact of the RSA on ratepayers, both present and future. Stated more generally, it is the

¹The withdrawal of this finding is not an admission that its use of the term "burden of proof" in paragraph 206 is inappropriate. The Commission finds, however, that the use of the term creates more confusion than light, and is not necessary to : explain the RSA proceeding.

Commission's obligation to establish just and reasonable rates; it is MPC's burden to convince the Commission that approval of the RSA is consistent with a finding that the rates established are just and reasonable. To meet this burden MPC must be convincing, not only in its initial filings, but in its responses to Commission and intervenor inquiries.

52. Second, the Commission has reached no decision, or formed any conclusion with respect to the proper ratemaking treatment of the RSA. Therefore, MPC's contention that the Commission's Order requires MPC to prove a negative (as in an order to show cause) is without merit. Paragraph 206 simply explains that the Commission is treating the RSA as a reserved issue in Docket No. 90.6.39, and establishes a procedure for exploring that issue. To the extent that MPC interprets the fifth sentence of paragraph 206, beginning with "It must also demonstrate....," as direction to prove a negative, the Commission withdraws that sentence and replaces it as indicated below. The Commission finds that Sections 69-3-321 and 69-3-324, MCA, are not relevant to this proceeding.

53. Third, the Commission withdraws the third sentence of paragraph 206, which reads, "Accordingly, MPC is directed to file, on [January 30, 1992], testimony and exhibits which quantify such impacts." In lieu of the direction to file testimony and exhibits, the Commission invites MPC to respond by January 30, 1992, in whatever manner it deems appropriate, and with whatever supporting documentation it feels is necessary, to the questions raised and concerns expressed in paragraph 206, as further described below². By taking this opportunity MPC will

²The Commission prefers prefiled testimony because it makes

expedite a decision on this issue. If, however, MPC chooses to rest on the testimony and material it has already presented on this issue, then it can expect to answer these questions and concerns (and perhaps others) in response to data requests from the Commission staff and intervenors. Such data requests will issue pursuant to the procedural order established subsequent to January 30, 1992.

54. Fourth, with respect to MPC's objection that paragraph 206 is vague and does not adequately inform MPC of the Commission's questions and concerns, the Commission explains, expands, and clarifies paragraph 206 as follows: The Commission does not know what the impacts of the RSA are on the operations of electric utility property that is dedicated to serve Montana ratepayers. Further, the Commission does not know the life cycle ratemaking impacts of the RSA. In order to answer these questions, the Commission must, at a minimum, be able to quantify all potential costs and benefits of the RSA (to the extent these can reasonably be identified) which will accrue from the date of this Order until the projected termination of the RSA, to the Montana electric utility and the CS4LMD. Accordingly, MPC must calculate the fully allocated life cycle costs of Colstrip 3 and Colstrip 4 (individually) for the above-described period. MPC should provide a narrative description of the life-cycle cost analysis. MPC should also address whether it explored an RSA for

the hearing process easier and it identifies a person to whom staff and intervenors can direct questions.

50 percent of Colstrip 3 output with other, nonaffiliated entities. Similarly, MPC should explain why there is an RSA with

Colstrip 4 in particular. In addition, MPC should analyze and explain whether the reduction in risk which it claims will accrue to the electric utility has any impact on its cost of capital.

WIM

55. MPC seeks limited reconsideration of the Washington, Idaho, Montana (WIM) issues which Order No. 5484k addresses on pages 85-90. The Order requests quarterly reports on all activities between the three utilities in question. MPC wants to exempt "routine" activities, such as spot market transactions within the WIM group.

56. The Commission finds that the findings in Order No. 5484k are still valid. MPC must report on all transactions and activities which occur between the entities in question. If it becomes apparent that the routine activities referenced by MPC have no bearing on other activities within the group, the Commission will consider changing the requirement that such information be provided. Until such time, documentation of routine activities may be filed in summary form.

Conservation Amortization

57. HRC stated that amortization and cost effectiveness are unrelated and should not be linked. HRC indicated that the last two sentences of Finding of Fact 220 should be struck.

58. MCC stated that the Commission should not conclude that "projects which have a payback period of more than ten years will not be considered cost effective." Payback and amortization periods need not be so linked. Cost effectiveness should be judged over a reasonable life for the investment. If the payback and amortization periods are so linked, the shorter amortization

period may actually create an unintended disincentive to make conservation investments.

59. MPC asked that the Commission reconsider its statement in Finding of Fact 220 that "projects which have a payback period of more than ten years will not be considered cost effective." According to MPC that decision could have adverse impacts on the amount of cost effective conservation available to MPC.

60. After due consideration the Commission finds that the comments of the parties are in agreement with respect to the last two sentences of Finding of Fact 220. The Commission grants the Motions for Reconsideration with respect to the last two sentences of Finding of Fact 220, and those sentences are hereby deleted. Removal of those two sentences in no way alters MPC's burden with respect to demonstrating that all conservation expenditures are cost effective.

Accounting Records for Conservation Expenditures

61. MPC asked that instead of mandating certain types of detailed records, the Commission mandate instead that the utility meet with the Commission staff to resolve the type and degree of detailed accounting records which should be kept on conservation resources. The Commission is agreeable to the proposal made by MPC. MPC is directed to meet with the Commission staff on the proper degree of accounting records which should be kept for conservation resources.

Hauser PS&I Costs

62. HRC asked in its Motion for Reconsideration that the Commission modify Finding of Fact 228 in Order No. 5484k to make clear that in the future it will critically review the prudence of the utility's site-specific preliminary investigation and

survey expenses. The Commission declines to modify Finding of Fact 228 as requested by HRC. The contents of that finding make it clear to MPC that future preliminary investigation and survey expenses will be carefully examined before those expenses are allowed into rates. The Motion for Reconsideration by HRC on the subject of preliminary survey and investigation expenses is denied.

Refunds and Settlements

63. MPC asked that the Commission reconsider its decision that natural gas settlements would no longer be included in gas trackers. MPC requested that the Commission reconsider this decision and explicitly consider it as part of a Notice of Inquiry. The Commission finds that the decision reached on the issue of gas settlements is appropriate given the past asymmetrical treatment of refunds and settlements and finds that the Motion for Reconsideration by MPC is denied.

Fog Wire

64. MCC states that the Commission's decision to revisit this issue is similar to the decision to revisit the Colstrip 4 RSA. MCC requests that the Commission consider affording interim treatment to the Fiber Optic Ground Wire (FOG Wire) revenues similar to the interim treatment afforded the \$650,000 RSA benefit.

65. MPC disagrees that interim treatment is proper. MPC states that the record contains no support for such treatment nor does MCC's motion. MPC contends it is entitled to a final order and that there is no basis to create uncertainty about this issue until a final decision in the next rate case. MPC claims that the same defect affects the RSA issue but that because the issue will

be resolved in the near future, the RSA can be differentiated from the FOG Wire issue.

66. MPC's claim that there is no basis for uncertainty about this issue is without merit. There already exists a great deal of uncertainty about this issue and the Commission has declined to draw final conclusions as a result. (Order No. 5484k, FOF No. 255) In recognition of MPC's concerns regarding a definite end to the uncertainty, the Commission is willing to speed-up resolution of this issue. Therefore, the FOG Wire issue will be considered a reserved issue to be addressed in the same manner and at the same time as the RSA issue.

67. In most instances, the record established before the Commission will include sufficient information to allow final resolution of the issues presented. That is not the case with the FOG Wire issue. The record established in this case does not convince the Commission that the revenues received by MPC in this affiliated interest transaction are sufficiently compensatory.

68. It is the Commission's duty to fairly balance the interests of MPC and its customers. The Commission believes interim treatment of this issue is the best means available to provide that required balance. Without interim treatment, customers are potentially disadvantaged due to the loss in purchasing power associated with the time value of money. If the final resolution of the issue is to accept the current level of FOG Wire revenues, then neither MPC nor its customers will have been disadvantaged by such interim treatment. If the final resolution of the issue results in recognizing higher FOG Wire revenues, the customers will receive interest on the difference, negating the potential for disadvantage.

69. The Commission views interim treatment to be a conservative approach which fairly protects the interests of MPC and its customers. MCC's motion is granted. Interest shall be accrued at 12.1 percent in the event higher FOG Wire revenues are determined to be appropriate. Such interest, if applicable, would begin to accrue on the approval date of this Order.

70. MPC is invited to respond, by January 30, 1992, in whatever manner it deems appropriate and with whatever documentation it feels necessary, to the general question of whether adequate compensation was received in the FOG Wire transaction. MPC is referred to Order No. 5484k, paragraphs 246-255. As with the RSA, MPC can rest with the information already submitted; but it can expect data requests on this subject following January 30, 1992.

Natural Gas Compressor Annualization

71. On pages 12 and 13 of its Motion for Reconsideration, the MCC requests reconsideration of the natural gas compressors annualization issue. The issue was dealt with on pp. 152-156 of Order No. 5484k.

72. The MCC's main disagreement with compressor annualization involves the aggregation concept used by the Commission to justify such annualization:

Even MPC did not attempt to aggregate from one rate case to the next rate case. If the compression was such an integral part of the project, then perhaps the 'phase-in' concept adopted by the Commission (that the project has been taken into rates in phases in three separate rate cases) should be viewed as having allowed CWIP (i.e., an unfinished project that did not include the compression) in rate base in Docket No. 88.6.15. In fact, adding compression to already operational facilities should not be viewed as a phase-in any more than adding an additional leg of transmission onto the

existing integrated transmission system would be viewed a phase-in. The Commission should reconsider this unwarranted erosion of the average rate base methodology.

73. The MPC responds that phased rate basing is proper in the context of the used and useful statute:

The MCC argument would mean that it would be impossible to find that part of a total project was use and useful (even though it was actually providing service) until all parts of the project of facility were fully operating. This interpretation would have to ignore the used and useful statute. It is ridiculous to assert that parts of the same project can never be put into service in increments and, thus, become used and useful in pieces. Yet, that is the MCC argument, and it must be rejected as failing any logical scrutiny because it is very possible, as in this case, that pieces of one project can and logically should be put into service at different times.

74. The Commission finds that both parties have valid concerns. MPC is right in its opinion that ratepayers may be well served if a large project can be phased into rates when discrete elements of the project are completed and become used and useful in the provision of service. For example, one may envision the construction of Colstrip 5 where the settling pond, water transmission line, or coal handling facilities were completed before the generating and turbine facilities. If one of the intended uses of such facilities were to provide backup reliability for Colstrip Units 1-4, it may be that MPC would seek rate base treatment for them before power was generated from Colstrip 5. A further extension of this reasoning may suggest that rate treatment could be sought even if backup reliability for Colstrip 1-4 were not contemplated. Such reasoning would come from a present value analysis which would demonstrate that

phasing Colstrip 5 facilities into rates would be the most cost effective way of supplying the energy demands of customers.

75. The MCC motion expresses a caution that has merit. The CWIP analogy expressed in its motion implies that the Commission must be very careful to ensure the used and usefulness of facilities for which phased in rate base treatment is sought. Used and usefulness over the life of the facilities is particularly relevant in this regard. The Commission is not aware of any used and useful concerns which have been expressed in this Docket.

76. The Commission finds, on balance, that the reasoning in Order No. 5484k is valid, and that its findings regarding this issue should not be changed. However, MPC must demonstrate more conclusively the life cycle present value cost-effectiveness of a project in its entirety before the Commission will consider the phased rate basing of future plant additions.

CONCLUSIONS OF LAW

1. All Findings of Fact are hereby incorporated as Conclusions of Law.

2. The Applicant, Montana Power Company, furnishes electric and gas service for consumers in the State of Montana, and is a "public utility" under the regulatory jurisdiction of the Montana Public Service Commission. Section 69-3-101, MCA.

3. The Montana Public Service Commission properly exercises jurisdiction over Montana Power Company's rates and operations. Section 69-3-102, MCA, and Title 69, Chapter 3, Part 3, MCA.

4. The Montana Public Service Commission has provided adequate public notice of all proceedings, and an opportunity to

be heard to all interested parties in this Docket. Sections 69-3-303, 69-3-104, MCA, and Title 2, Chapter 4, MCA.

5. Subject to a determination on the reserved issues discussed in this Order, the rate level approved herein is just, reasonable, and not unjustly discriminatory. Sections 69-3-330 and 69-3-201, MCA.

ORDER

THE MONTANA PUBLIC SERVICE COMMISSION HEREBY ORDERS:

1. All Motions for Reconsideration of Order No. 5484k are disposed of as described above.

2. The revenue requirement determined in Order No. 5484k, for both the gas and electric utilities, does not change as a result of this Order.

3. With the two exceptions noted below, the Commission's decisions on all revenue requirement issues in this Docket are final.

4. The proper ratemaking treatment of both the reciprocal sharing agreement and the fiber optic ground wire transaction is reserved to a later proceeding in this Docket. The Commission's decisions on these issues are interim pending that proceeding.

DONE AND DATED this 7th day of November, 1991, by a 5 to 0 vote.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

HOWARD L. ELLIS, Chairman

DANNY OBERG, Vice Chairman

WALLACE W. "WALLY" MERCER, Commissioner

JOHN B. DRISCOLL, Commissioner

BOB ANDERSON, Commissioner

ATTEST:

Ann Peck
Commission Secretary

(SEAL)

NOTE: Any interested party may request that the Commission reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.

Acronyms List

CWIP	Construction Work in Progress
DCF	Discounted Cash Flow
FERC	Federal Energy Regulatory Commission
FOG Wire	Fiber optic Ground Wire
HRC	District XI Human Resource Council
IP	Idaho Power
LADWP	Los Angeles Department of Water and Power
LESOP	Leveraged Employee Stock Ownership Plan
MCC	Montana Consumer Counsel
MPC	Montana Power Company
RSA	Reciprocal Sharing Agreement
WECo	Western Energy Company
WIM	Washington, Idaho, Montana
WWP	Washington Water Power